



GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

Fiscal Note 2017 Biennium

| | | | |
|-------------------------|-------------------|----------------|--|
| Bill # | HB0420 | Title: | Revise oil and gas tax rates and increase distributions to local governments |
| Primary Sponsor: | Dunwell, Mary Ann | Status: | As Introduced |

- | | | |
|--|--|--|
| <input checked="" type="checkbox"/> Significant Local Gov Impact | <input checked="" type="checkbox"/> Needs to be included in HB 2 | <input checked="" type="checkbox"/> Technical Concerns |
| <input type="checkbox"/> Included in the Executive Budget | <input type="checkbox"/> Significant Long-Term Impacts | <input type="checkbox"/> Dedicated Revenue Form Attached |

FISCAL SUMMARY

| | <u>FY 2016 Difference</u> | <u>FY 2017 Difference</u> | <u>FY 2018 Difference</u> | <u>FY 2019 Difference</u> |
|---|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| Expenditures: | | | | |
| General Fund | \$16,100 | \$0 | \$0 | \$0 |
| State Special Revenue | \$0 | \$0 | \$0 | \$0 |
| Revenue: | | | | |
| General Fund | (\$7,759,629) | (\$5,475,202) | (\$4,941,758) | (\$4,926,551) |
| State Special Revenue | \$10,608,787 | \$11,455,863 | \$11,510,560 | \$12,087,117 |
| Net Impact-General Fund Balance: | <u>(\$7,775,729)</u> | <u>(\$5,475,202)</u> | <u>(\$4,941,758)</u> | <u>(\$4,926,551)</u> |

Description of fiscal impact: HB 420 changes the tax rate for the first 12 months of production for vertical oil and gas wells and the first 18 months of production for horizontal wells from 0.5% to 4.5%. It creates an additional distribution from the state portion of oil and gas revenue to incorporated cities and towns in oil and gas producing counties. This new distribution directs 10% of the state share of oil and natural gas tax revenue to cities and towns and is allocated among the entities based on population size. More revenue is distributed due to the increased holiday tax rate. Counties and state special revenue funds receive additional revenue from the provisions of this bill, while the state general fund experiences a reduction in revenue due to the increased distribution to cities and towns from the state share of revenue.

FISCAL ANALYSIS

Assumptions:

1. The current tax rate for working interest owners for the first 12 months of production from natural gas wells, primary recovery oil wells and the first 18 months of production from horizontally drilled natural gas and oil wells is 0.5%. HB 420 proposes to change the tax rate on these wells from 0.5% to 4.5%.

2. HB 420 creates a new distribution to oil and gas producing counties, which is 10% of the state share of oil and natural gas revenue. The counties would then distribute this revenue to incorporated cities and towns relative to their population size.
3. The allocation to cities and towns would reduce the amount of oil and natural gas tax revenue credited to the state general fund.
4. The proposed tax rate in HB 420 will affect revenue collections from the working interest portion of holiday oil and natural gas production. The value of the working interest portion of oil and natural gas production is assumed to be 82% of the total gross value of holiday oil and natural gas production.
5. Revenue estimates from HJ 2 (extrapolated using OBPP's growth rates for FY 2018 and FY 2019) are used to calculate the state portion of oil and natural gas tax revenue and the gross value of the working interest portion of holiday oil and natural gas production for the current law scenario.
6. The state portion of oil and gas revenue under proposed law is found by adjusting the revenue accruing from the working interest value of holiday oil and natural gas production for the higher tax rate provided for in HB 420. The state portion of oil and natural gas revenue is greater under the proposed law scenario due to the higher tax rate on holiday production.
7. Tables 1-4 show the difference between tax revenue and distribution under current law and the revenue and distribution that would result from the implementation of HB 420. The tables outline these scenarios for FY 2016 through FY 2019.

| Table 1 | | | |
|--|--------------------|---------------------|-------------------|
| FY 2016 Oil and Natural Gas Production Tax Revenue and Distribution | | | |
| | Current Law | Proposed Law | Difference |
| State Portion of Oil & Gas Revenue | \$100,452,228 | \$103,301,385 | \$2,849,157 |
| Natural Resource Projects Acct. | \$2,169,768 | \$2,231,310 | \$61,542 |
| Natural Resource Operations Acct. | \$2,029,135 | \$2,086,688 | \$57,553 |
| Orphan Share Acct. | \$2,963,341 | \$3,047,391 | \$84,050 |
| University System | \$2,661,984 | \$2,737,487 | \$75,503 |
| State Share to Cities and Towns | \$0 | \$10,330,139 | \$10,330,139 |
| General Fund | \$90,628,000 | \$82,868,371 | (\$7,759,629) |

| Table 2 | | | |
|--|--------------------|---------------------|-------------------|
| FY 2017 Oil and Natural Gas Production Tax Revenue and Distribution | | | |
| | Current Law | Proposed Law | Difference |
| State Portion of Oil & Gas Revenue | \$102,728,885 | \$108,709,546 | \$5,980,661 |
| Natural Resource Projects Acct. | \$2,218,944 | \$2,348,126 | \$129,182 |
| Natural Resource Operations Acct. | \$2,075,123 | \$2,195,933 | \$120,809 |
| Orphan Share Acct. | \$3,030,502 | \$3,206,932 | \$176,429 |
| University System | \$2,722,315 | \$2,880,803 | \$158,488 |
| State Share to Cities and Towns | \$0 | \$10,870,955 | \$10,870,955 |
| General Fund | \$92,682,000 | \$87,206,798 | (\$5,475,202) |

| Table 3 | | | |
|--|--------------------|---------------------|-------------------|
| FY 2018 Oil and Natural Gas Production Tax Revenue and Distribution | | | |
| | Current Law | Proposed Law | Difference |
| State Portion of Oil & Gas Revenue | \$102,112,512 | \$108,681,314 | \$6,568,802 |
| Natural Resource Projects Acct. | \$2,205,630 | \$2,347,516 | \$141,886 |
| Natural Resource Operations Acct. | \$2,062,673 | \$2,195,363 | \$132,690 |
| Orphan Share Acct. | \$3,012,319 | \$3,206,099 | \$193,780 |
| University System | \$2,705,982 | \$2,880,055 | \$174,073 |
| State Share to Cities and Towns | \$0 | \$10,868,131 | \$10,868,131 |
| General Fund | \$92,125,908 | \$87,184,150 | (\$4,941,758) |

| Table 4 | | | |
|--|--------------------|---------------------|-------------------|
| FY 2019 Oil and Natural Gas Production Tax Revenue and Distribution | | | |
| | Current Law | Proposed Law | Difference |
| State Portion of Oil & Gas Revenue | \$106,707,575 | \$113,868,142 | \$7,160,567 |
| Natural Resource Projects Acct. | \$2,304,884 | \$2,459,552 | \$154,668 |
| Natural Resource Operations Acct. | \$2,155,493 | \$2,300,136 | \$144,643 |
| Orphan Share Acct. | \$3,147,873 | \$3,359,110 | \$211,237 |
| University System | \$2,827,751 | \$3,017,506 | \$189,755 |
| State Share to Cities and Towns | \$0 | \$11,386,814 | \$11,386,814 |
| General Fund | \$96,271,574 | \$91,345,023 | (\$4,926,551) |

8. Tables 5-8 show the estimated increase in tax revenue for FY 2016 through FY 2019 from the working interest portion of holiday oil and gas production that will be manifest from the higher 4.5% tax rate proposed in HB 420. The higher tax rate on holiday production results in a greater amount of oil and natural gas tax due to the State of Montana overall. This increased revenue is shown in last column of tables 5-8. Since more tax is being paid by oil and natural gas producers, it translates to more money being available to counties and local governments as well as the State of Montana. For example, the \$5,062,267 estimated overall increase to oil and natural gas tax revenue in FY 2016 (table 5) results in a boost to the state share of revenue, a sum amounting to \$2,849,157 (table 1). The increase to the state share of revenue then flows through to the state special revenue funds (shown in tables 1-4). The numbers in tables 5-8 do not tie directly to any of the numbers in the *fiscal impact* or *fiscal summary* tables in this document, but serve to concisely show the estimated increase in tax oil and natural gas producers will pay to Montana.

| Table 5 | | | |
|---|--------------------|---------------------|-------------------|
| FY 2016 Change in Tax Revenue from Working Interest Value of Holiday Oil and Natural Gas | | | |
| | Current Law | Proposed Law | Difference |
| Resource Value | \$253,113,339 | \$253,113,339 | \$0 |
| Tax Rate | 0.5% | 4.5%* | 4.0% |
| Tax Revenue | \$1,265,567 | \$6,327,833 | \$5,062,267 |

*0.5% for the first half of FY 2016 and 4.5% for the second half.

| Table 6 | | | |
|---|--------------------|---------------------|-------------------|
| FY 2017 Change in Tax Revenue from Working Interest Value of Holiday Oil and Natural Gas | | | |
| | Current Law | Proposed Law | Difference |
| Resource Value | \$279,259,100 | \$279,259,100 | \$0 |
| Tax Rate | 0.5% | 4.5% | 4.0% |
| Tax Revenue | \$1,396,296 | \$12,566,660 | \$11,170,364 |

| Table 7 | | | |
|---|--------------------|---------------------|-------------------|
| FY 2018 Change in Tax Revenue from Working Interest Value of Holiday Oil and Natural Gas | | | |
| | Current Law | Proposed Law | Difference |
| Resource Value | \$308,127,315 | \$308,127,315 | \$0 |
| Tax Rate | 0.5% | 4.5% | 4.0% |
| Tax Revenue | \$1,540,637 | \$13,865,729 | \$12,325,093 |

| Table 8 | | | |
|---|--------------------|---------------------|-------------------|
| FY 2019 Change in Tax Revenue from Working Interest Value of Holiday Oil and Natural Gas | | | |
| | Current Law | Proposed Law | Difference |
| Resource Value | \$336,384,869 | \$336,384,869 | \$0 |
| Tax Rate | 0.5% | 4.5% | 4.0% |
| Tax Revenue | \$1,681,924 | \$15,137,319 | \$13,455,395 |

9. Under proposed law, the state share of oil and natural gas tax revenue is found by assuming that the counties and schools distribution is 46.12%, which is the percentage they received in FY 2014.
10. The additional revenue to be distributed to cities and towns under the proposed law is expected to be \$10,330,139 in FY 2016, \$10,870,955 in FY 2017, \$10,868,131 in FY 2018, and \$11,386,814 in FY 2019.
11. The additional revenue to be distributed to schools, for purposes of this fiscal note, would not be significant as the bill is written.
12. This bill would result in administrative costs of \$16,100 for the department in FY 2016.
13. This bill is effective October 1, 2015. It applies to oil and natural gas produced after December 31, 2015, the third quarter of FY 2016. Thus, holiday production in the first half of FY 2016 would have the same tax rate as current law, 0.5%. Holiday production in the second half of FY 2016 would have the new tax rate of 4.5%.

| | <u>FY 2016 Difference</u> | <u>FY 2017 Difference</u> | <u>FY 2018 Difference</u> | <u>FY 2019 Difference</u> |
|---|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| <u>Fiscal Impact:</u> | | | | |
| <u>Expenditures:</u> | | | | |
| Operating Expenses | \$16,100 | \$0 | \$0 | \$0 |
| TOTAL Expenditures | \$16,100 | \$0 | \$0 | \$0 |
| <u>Funding of Expenditures:</u> | | | | |
| General Fund (01) | \$16,100 | \$0 | \$0 | \$0 |
| State Special Revenue (02) | \$0 | \$0 | \$0 | \$0 |
| TOTAL Funding of Exp. | \$16,100 | \$0 | \$0 | \$0 |
| <u>Revenues:</u> | | | | |
| General Fund (01) | (\$7,759,629) | (\$5,475,202) | (\$4,941,758) | (\$4,926,551) |
| State Special Revenue (02) | \$10,608,787 | \$11,455,863 | \$11,510,560 | \$12,087,117 |
| Natural Res Proj Acct | \$61,542 | \$129,182 | \$141,886 | \$154,668 |
| Natural Res Operations | \$57,553 | \$120,809 | \$132,690 | \$144,643 |
| Orphan Share Acct | \$84,050 | \$176,429 | \$193,780 | \$211,237 |
| MUS | \$75,503 | \$158,488 | \$174,073 | \$189,755 |
| Cities and Towns | \$10,330,139 | \$10,870,955 | \$10,868,131 | \$11,386,814 |
| TOTAL Revenues | \$2,849,158 | \$5,980,661 | \$6,568,802 | \$7,160,566 |
| <u>Net Impact to Fund Balance (Revenue minus Funding of Expenditures):</u> | | | | |
| General Fund (01) | (\$7,775,729) | (\$5,475,202) | (\$4,941,758) | (\$4,926,551) |
| State Special Revenue (02) | \$10,608,787 | \$11,455,863 | \$11,510,560 | \$12,087,117 |

Effect on County or Other Local Revenues or Expenditures:

1. Incorporated cities and towns in oil and gas producing counties would receive additional funding under this bill. The estimated amounts are provided in tables 1-4 and in assumption 10.
2. Counties and schools would also receive additional funding from the increase in oil and gas production tax revenue. These amounts are estimated at \$6.1 million in FY 2016, \$7.3 million in FY 2017, \$7.9 million in FY 2018, and \$8.1 million in FY 2019.

Technical Notes:

1. Please see line 24 page 4 of the bill under 15-36-331, MCA. New language may need to be added to include after the word oil “and gas” producing county.
2. Administrative rules may be needed to determine how the department will determine the amount of money going to the cities and towns.

*Sponsor's Initials*_____
*Date*_____
*Budget Director's Initials*_____
Date